

## NECPUC GOVERNANCE PRINCIPLES AND PROPOSAL

### Basic Principles

1. Market participants (as well as regulators) are entitled to a full opportunity to be heard on decisions that may affect them.
2. The decisions concerning market rules to be administered by the RTO are FERC decisions.
3. The RTO should not be, and should not be regarded as, a “partner,” an offspring, or a contractor of the market participants. The whole idea of the RTO is to create an entity that is sufficiently independent of all market participants that FERC can allow a market to exist (and can assume that market can replace cost-based ratemaking) without constant and detailed intervention. Where, as is clearly the case today, public confidence in market participants to act in the public interest rather than their own pecuniary interests is low, direct control in any form over the management or operation of the RTO is likely to compromise public acceptance and support for "competitive" electricity markets.
4. The role of the RTO is to administer tariffs and markets pursuant to FERC approved rules. The RTO’s role is not to set policy, but to ensure that FERC has the benefit of the expertise and recommendations of a genuinely independent but nevertheless fully involved entity with no allegiance except to fulfilling the operational and market role given by FERC.

### Implications Of These Principles

1. Any ability of any market participant, or group or organization of market participants, to direct the operations, governance, management, budget or positions taken by the RTO is fundamentally contradictory to the essential independence of the RTO. The RTO must be permitted to exercise its unfettered judgment in carrying out its tasks. Recourse by disappointed market participants (and regulators) must be to FERC – not through influence on the board, management or budget of the RTO.
2. The RTO Board must be, fundamentally, FERC-selected. This does not mean that FERC organizes the search for new members. It means that the FERC has the final say over the approval of board members selected by the existing board members. If FERC has the final say over board appointments, the Board is not “self-perpetuating.” In fulfilling its board selection role, the RTO board is merely acting in its appropriately independent and FERC supervised capacity. Any degree of market participant control (even, as discussed below, if that control is exercised by voting for a slate of board candidates) will compromise the ability of the RTO to act as the independent agent necessary to ensure a market adequately insulated from undue market participant influence.

## Answers To Objections

1. The RTO won't be accountable.

Answer: The RTO's role is defined by FERC, and FERC (with appropriate input from all sectors) should decide if the RTO is behaving properly and functioning efficiently. In contrast with FERC, market participants have a fiduciary responsibility to their shareholders, not to the market per se or to customers as a whole. There is no reason to doubt that FERC will address any legitimate concerns of market participants while protecting the interests of those who are affected by the market but not adequately represented by the market participants.

2. Without the power to direct RTO actions, the market participants will lose interest.

Answer: Why? The money will still be in play. Coalitions of interest rise and fall all the time. Nothing would prevent, or discourage, market participants from organizing as they see fit to ensure that their positions were articulated clearly and forcefully.

3. Without a hammer held by NEPOOL (or equivalent), the RTO will ignore good advice.

Answer: Conceptually, this is unlikely: since disappointed participants have access to FERC, repeated close-mindedness by the RTO will lead to FERC intervention. Empirically, there is no evidence of this: the NE-ISO has rarely gone contrary to the expressed wishes of the full breadth of market participants' interests and those instances of disagreement involved disputes over authority and timing of actions rather than the substance of the filing itself. Failure to follow the advice of market participants, or factions of market participants, does not indicate a failure to discharge ISO or RTO responsibilities. Such "failure" is as likely to be evidence that the ISO or RTO is taking into account the interests of those who are underrepresented (e.g. residential and small business consumers) in the market participants' forum.

How can the legitimate interests of the market participants be accommodated without giving them "directing" power over the RTO?

1. Provide a willing ear.

The RTO can commit to give appropriate notice of actions it is considering, and to articulate the basis for any decision and why losing positions were rejected.

2. Ensure access to FERC.

This is not the RTO's to "give," but it might be reasonable to suggest to FERC that the FERC will, when a sufficient number (or critical mass) of market participants object to an RTO action (ex ante or ex post), consider the merits of the non-RTO arguments notwithstanding any deference that might otherwise be given to the RTO's § 205 filing.

**Why A Market Participant Vote On A Slate Of Board Candidates Will Compromise Board Independence**

1. Providing market participants with the authority to approve or disapprove a slate of candidates will give market participants the right to veto any candidate who does not suit the majority of market participants. Even with "all or nothing" voting, it would be easy to identify the "blackballed" candidate or candidates.
2. Market participants could prevent the Board from filling vacancies on the Board and thus prevent the Board from operating efficiently. The institutional gridlock caused in the past by "sharing control" with market participants should not be "hard-wired" into a new organizational structure.
3. The problem with independence persists whether the market participants "approve" the slate by a simple majority or whether a higher threshold is required.
  - a. While a simple majority vote from market participants could relieve "gridlock," it would facilitate dominance by an even less representative segment of those affected by RTO decisions.
  - b. A higher threshold would likely create the kind of decisional paralysis that has characterized NEPOOL decision making in the past.
4. Both actual and perceived independence are crucial in maintaining consumer confidence in wholesale electricity markets. The RTO is the entity which the FERC has chosen to develop and operate wholesale electricity markets and to ensure that they operate efficiently and competitively. If there is a question about whether the markets are operating competitively, consumers will not have confidence in the assurances of an entity that appears to be elected by those whose market behavior may be in question. Allowing a group of market participants to select or approve RTO board members poses the same dangers as would exist if they were allowed to select or approve FERC Commissioners.

## **Governance Proposal**

### **Board Member Selection**

NECPUC endorses the following proposal for Board member selection and re-election:

- a. The ISO-NE and NYISO Board would select five members each from its respective boards. The five members would represent a range of expertise that would be identified in advance (similar to criteria established for the current board).
- b. The Board should seek regulator and market participant input before selection.
- c. The ISOs would then seek FERC confirmation of the 10 new Board members. Market participants and regulators may comment to FERC on the proposed board members.
- d. FERC would confirm or reject new board (since FERC has the ultimate authority and obligation to ensure that the markets are operating competitively, it is the logical entity to confirm or veto Board member selections made by the Board).
- e. The new RTO Board would select three additional members through a nominating committee formed from existing Board members. The process for selection would then follow the process described in b through c.
- f. The same process described in e would be used for re-election of Board members. Initial Board members would have staggered three and four year terms. Subsequent terms would be for three years
- g. Removal only for good cause and by a simple majority of Board members
- h. CEO is non-voting member of the Board
- i. Although this proposal does not specifically address term or age limits, NECPUC would not necessarily oppose reasonable efforts to ensure some degree of turnover in the Board.

While the model set forth above is NECPUC's preferred option because it avoids any *appearance* of compromising ISO independence, NECPUC could accept a model that had limited minority representation by market participants and state regulators on the nominating committee. For example if the nominating committee had nine members, five would be existing board members, two would be market participant members and two would be state regulators. A third alternative would be to have a minority of market participants on the nominating committee who would select a slate of nominees from a larger pool of candidates chosen by state regulators.

## **Section 205 Filing Rights**

The Board would have sole authority to propose market rules and make amendments to market rules without any mandatory waiting period to accommodate Market Participant approval of the proposal. However, the RTO Board would seek input from stakeholders in developing the rules and its FERC filing must include discussions of the input it received from stakeholders. In addition, if market participants have a different proposal than that proposed by the RTO Board, the ISO must include and discuss this option in its section 205 filing. The ISO is not, however, required to delay its FERC filing to allow market participants to formulate a position on the proposed rules or rule amendments.

## **RTO Purpose**

Board members must have a fiduciary obligation and purpose devoted to the public interest (as adequate substitute for the statutory "just and reasonable rate" requirement) with particular reference to the following:

- system reliability and operating efficiency
- efficiently functioning markets that operate fairly and provide a balance between the concerns of buyers and sellers
- balance between short-term and long-term objectives.

## **RTO Functions**

1. Propose market rules and amendments under section 205 of the FPA for the purpose of ensuring that the RTO markets operate efficiently and competitively and do not provide opportunities for the exercise of anti-competitive behavior.
2. Operate the RTO dispatch and transmission system, securely, reliably and efficiently.

## **RTO Funding**

The RTO files a tariff at FERC. The tariff is not subject to stakeholder approval but the RTO will seek input from stakeholders prior to filing the tariff at FERC.